91-745

No. A - 59

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1991

James and Nancy L. Karr, Petitioner

v.

Commissioner of Internal Revenue,
Respondent

PETITION FOR WRIT OF CERTIORARI TO THE

11TH CIRCUIT COURT OF APPEALS

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Whether the 11th Circuit's use of the clearly erroneous standard in reviewing the Tax Court's determination that the Koppelman Process was an economic sham was improper?

2. Whether, in determining if POGA's activities lacked economic substance, the 11th Circuit's improperly focused on the wisdom of investing in the Koppelman Process as viewed with hindsight?

3. Whether, as a matter of law, the 11th Circuit's consideration of the testimony of POGA's attorney, Michael Zukerman, in determining the economic substance of the Koppleman Process was erroneous?

4. Whether the 11th Circuit's determination that interest expense accrued by POGA was not deductible because the interest on the obligations was too contingent was erroneous?

5. Whether the 11th Circuit's determination that the Commissioner of Internal Revenue did not abuse his discretion by failing to waive the addition to tax pursuant to Internal Revenue Code section 6661 was incorrect?

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OPINIONS BELOW

The opinion of the 11th Circuit is reported at 924 F.2d 1018 (1991), 91-1 U.S.T.C. para. 50,113, and is reprinted as Appendix A, hereto. The opinion of the United States Tax Court is reported at 91 T.C. 733 (1988), and is reprinted as Appendix B herto. A supplemental opinion of the Tax Court is reported at 93 T.C. 378 (1989). That opinion, however, is not relevant to the questions presented to this Court.

JURISDICTION

This Court has jurisdiction to review the judgment of the United States Court of Appeals for the 11th Circuit entered on February 27, 1991 pursuant to Title 28, United States Code, Section 1254. A copy of the judgment is

reprinted as Appendix E, hereto. A timely petition for rehearing by the 11th Circuit was denied on May 7, 1991. A copy of the order denying the petition for rehearing is reprinted as Appendix D hereto. On July 18, 1991, Associate Justice Anthony M. Kennedy issued an order extending the time for filing a petition for a writ of certiorari to and including October 2, 1991.

STATUTES INVOLVED

The statute principally involved is section 6661. The full text of the statute is reprinted as Appendix F, hereto.

STATEMENT OF THE CASE

James and Nancy L. Karr (the "taxpayers") bring this appeal from the decision of 11th Circuit Court of Appeals which affirmed the decision of the United States Tax Court entered on September 29, 1989. The Tax Court had jurisdiction of the case pursuant to sections 7442, 6213 and 6214 of the Internal Revenue Code of 1986.

The opinion of the Tax Court on which the decision was based found that the taxpayers were not entitled to deduct their pro rata share of the losses incurred by Peat Oil and Gas Associates, Ltd. ("POGA") deducted by them on their 1981 and 1982 income tax returns, except as to certain amounts conceded by the Commissioner of Internal Revenue related

to expenses of oil and gas drilling activities. In addition, the Tax Court held that the taxpayers were liable for an addition to tax pursuant to section 6661.[1] The Karrs' case was consolidated and tried with that of Dean and Irma Smith, limited partners of Syn-Fuel Associates, Ltd. ("SFA").

The Tax Court issued a joint opinion applying to both the Smiths and the Karrs. The Smiths appealed the Tax Court's decision to the 6th Circuit Court of Appeals, and on June 27, 1991 the 6th Circuit issued its opinion reversing the decision of the Tax Court in its entirety, and remanding the case to the Tax Court for further proceedings on the

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[1] All section references except as otherwise indicated are to the Internal Revenue Code of 1954 as in effect during the years at issue.

remaining issue. The 6th Circuit's opinion is reproduced as Appendix C. The government has not filed a petition for certiorari in the Smith case, and the time for doing so expired on Sept. 25, 1991.

The underlying facts are as follows. In 1981 James Karr became a limited partner in POGA, and Dean and Irma Smith became limited partners in SFA. SFA and POGA (collectively the "Partnerships") were formed for the purpose of (i) engaging in the exploration and development of oil and gas prospects and the acquisition and ownership of oil and gas interests; (ii) owning, licensing or otherwise exploiting technology relating to the production of synthetic fuel from peat and other cellulosic materials; and (iii) experimenting, utilizing and

licensing technology, in an attempt to demonstrate the commercial feasibility of producing synthetic fuel from peat and other cellulosic materials, including constructing, operating and managing a pilot plant that would attempt to convert peat and other cellulosic material into synthetic fuel, and if successful, commercially producing synthetic fuel from peat and other cellulosic materials.

In 1981 the Partnerships entered into a joint venture agreement to own, operate, and manage a pilot K-Fuel plant (the "North Carolina Plant"). K-Fuel is a dry, stable, high heating value solid fuel, physically resembling coal which is produced by placing wood, peat, lignite and other low grade biomass or fossil fuel into a Koppelman Reactor, where it is dried and carbonized at high

temperatures and pressures (hereinafter the "Koppelman Process"). K-Fuel has a low ash and sulfur content, and is therefore environmentally highly desirable. It can be mixed with water and with certain modifications can be burned in oil fired boilers.

The Koppelman Process was developed by Edward Koppelman ("Koppelman"), and has been favorably reviewed and extensively written about in various technical and industry journals. In 1980, the United States Department of Energy awarded Koppelman a $727,882 grant to study the feasibility of the Koppelman Process. Pursuant to the grant, Koppelman, SRI International ("SRI")[2],

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[2] SRI is a leading research and development organization that provides research and consulting for business and government clients worldwide.

the University of Maine, Lehman Brothers Kuhn Loeb, Inc., Ekono, Inc., Central Maine Power Company, and Stone and Webster Engineering Corporation ("Stone and Webster")[3] prepared a report. The report concluded that the Koppelman Process was "technically, environmentally, and economically feasible".

By the summer of 1981, Koppelman together with SRI had built a model plant capable of producing K-Fuel in small quantities. In August of 1981, Ronodo Corporation, N.V., ("Ronodo") licensed from Koppelman the exclusive right to use the Koppelman Process within the State of North Carolina to refine peat and wood

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[3] Stone and Webster has a reputation as a leader in the engineering field with respect to the construction of large scale plants.

into K-Fuel, as well as certain additional rights. All of these rights were sublicensed by Ronodo to its wholly owned subsidiary, Sci-Teck Licensing Corporation ("Sci-Teck").

At the end of 1981, the Partnerships licensed from Sci-Teck the exclusive rights within the State of North Carolina to use the Koppelman Process with respect to peat and wood, as well as the non-exclusive right to use the Koppelman Process in the remainder of the United States with respect to any material other than bagasse. The Partnerships agreed to pay a license fee to Sci-Teck which included both cash and partnership notes. Specifically, for each partnership unit sold the Partnerships agreed to pay a license fee to Sci-Teck of $12,175 in cash between October 1, 1981 and Oct 1,

1984, and $99,200 of promissory notes due between October 1, 2006 and 2009.

At the same time the Partnerships entered into research and development agreements with Fuel-Teck Research and Development ("FTRD"). FTRD's role was to conduct and coordinate the research and development efforts of Koppelman, A.T. Kearney and others for the benefit of the Partnerships, and to oversee the construction by Stone & Webster of the North Carolina Plant. The purpose of building the North Carolina Plant was to determine if it was possible to build a K-Fuel plant capable of producing K-Fuel in commercial quantities. The Partnerships agreed to pay FTRD a fee for its services which included both cash and partnership notes. The structure of this payment required the Partnerships to pay

FTRD $5,000 in cash between October 1, 1981 and October 1, 1982, and $24,800 in promissory notes due between October 1, 2006 and October 1, 2007 for each partnership unit sold.

The notes due to both Sci-Teck and FTRD were to be prepaid out of any partnership revenues, including revenues from the Partnerships' oil and gas wells. Furthermore, each limited partner including the Karrs agreed to assume a pro rata share of the principal balance of the Partnerships' liabilities to Sci-Teck and FTRD. By 1984 the Partnerships had built the North Carolina Plant, but due to a combination of technical difficulties and the falling price of energy no revenues were ever generated from the licensing of the Koppelman Process.

REASONS FOR GRANTING THE WRIT

This case presents a conflict between decisions of the Sixth and 11th Circuit Courts of Appeals which were based on identical facts. The outcome of this case will directly affect the outcome of the cases of approximately 300 individuals who are limited partners of POGA, SFA and a related third partnership, Syn-Fuel Associates, 1982. The case is an opportunity to resolve a conflict among the circuits as to the proper standard of review of a finding that a transaction is an economic sham. It also presents an opportunity for this Court to correct the 11th Circuit's decision which is not consonant with the opinion of this Court in United States v. Boyle, 469 U.S. 241, 105 S.Ct. 687 (1985).

I. <u>The Eleventh Circuit Should Have Reviewed De Novo the Tax Court's Determination That the Koppelman Process Activities Lacked Economic Substance.</u>

The 11th Circuit held that the question of whether or not a transaction is an economic sham is subject to the clearly erroneous standard of review. Three other circuits have held that this question should be reviewed <u>de novo</u>. <u>James v. Commissioner</u>, 899 F.2d 905, 909 (10th Cir. 1990); <u>Newman v. Commissioner</u>, 894 F.2d 560, 562 (2d Cir. 1990); <u>Killingsworth v. Commissioner</u>, 864 F.2d 1214, 1217 (5th Cir. 1989); <u>contra</u> <u>Ratliff v. Commissioner</u>, 865 F.2d 97, 98 (6th Cir. 1989); <u>Casebeer v. Commissioner</u>, 909 F.2d 1360 (9th Cir. 1990).

Furthermore, the decision of the 11th Circuit is in conflict with prior decisions of this Court. In Knetsch v. United States, 364 U.S. 363, 365, 81 S. Ct. 132, 134 (1960), this Court referred to the characterization of a transaction as a sham, as a conclusion of law. In Frank Lyon Co. v. United States, 435 U.S. 580, 581 at n. 16, 98 S.Ct. 1291, 1302 (1978) in reviewing whether or not the form of a transaction should be respected this court stated, "[t]he general characterization of a transaction for tax purposes is a question of law subject to review. The particular facts from which the characterization is to made are not so subject." [citation omitted]. Indeed, in Casebeer v. United States, 909 F.2d at 1362, n.6 the 9th Circuit noted that its decision to apply the clearly erroneous

standard appeared to be inconsistent with Frank Lyon Co.

II. The Eleventh Circuit Improperly Focused on the Wisdom of Investing in the Koppelman Process as Viewed in Hindsight.

On identical facts as those examined by the Sixth Circuit, the 11th Circuit held that the Koppelman Process activities of the Partnerships were a sham. Both the Sixth and Eleventh Circuits purported to use the same standard in determining whether the transactions had economic substance, i.e. whether the transactions had any practicable economic effect other than the creation of tax losses. However, the Sixth Circuit noted that the Tax Court had improperly focused on whether, in hindsight, the investment was a wise one

rather than whether or not it was bona fide. The 11th Circuit's analysis was similarly improperly slanted.

The only evidence in the record concerning the objective possibility of economic success was the testimony and report of the taxpayers' experts, Drs. Plummer and Thomas. It was their uncontradicted and unimpeached testimony that viewed from the date of the Partnerships' inception, there was a reasonable possibility of profit in the range of 25 to 40 per cent. Furthermore, the Internal Revenue Service hired their own experts, and then vigorously and successful opposed the taxpayers' efforts to call those experts to testify. At no point in its opinion did the Tax Court find fault with the opinion of the taxpayers' experts. It was only by

viewing the transaction in hindsight and substituting its own business judgment for that of the Partnerships' that the 11th Circuit could rule that the Karrs were not entitled to rely on this expert testimony.

The 11th Circuit found that the testimony of the experts was flawed since they assumed that the Koppelman Process would be commercially successful, and failed to consider the risk factors set forth in the POGA offering memorandum. The infirmities of this conclusion are severalfold. Dr. Plummer explained that the risk factors were taken into account by requiring a higher rate of return on a risky project. In government counsel's cross examination of Dr. Plummer, he attempted to establish that the risk factors had not been taken into account,

and that the so-called expected value method would have been more appropriate. The Tax Court specifically stated at trial, however, that there was "no evidence on which to base any kind of finding that the expected value method would have been preferable...."

The Tax Court found, in its opinion, that "[i]n determining whether the price paid by the partnerships for licensing the technology was reasonable, Plummer and Thomas compared the rate of return sought by the partnerships to that sought by Occidental Petroleum in a much larger and riskier shale oil project in Colorado." Thus, the Tax Court's own finding leaves no room for the 11th Circuit's conclusion that the Tax Court was entitled to ignore the experts' testimony because it failed to consider

the risk factors. Indeed there was no finding by the Tax Court that the expert testimony was in anyway impaired. The court may not ignore expert testimony which is unimpeached, competent and uncontradicted. Tank v. Commissioner, 270 F.2d 477, 487 (6th Cir. 1959) (concurring opinion). See, Akers v. Commissioner, 798 F.2d 894 (6th Cir. 1986) rev'g and remanding T.C.M. 1984-207 (Tax Court may not choose to ignore expert testimony without an explanation of its rationale).

III. THE ELEVENTH CIRCUIT ERRED IN NOT HOLDING THAT THE TESTIMONY OF THE PARTNERSHIPS' ATTORNEY MICHAEL ZUKERMAN IS IRRELEVANT TO A DETERMINATION OF THE PROFIT MOTIVE OF THE PARTNERSHIPS.

In determining the existence of a

profit motive an examination of the appropriate factors is made at the partnership level. Brannen v. Commissioner, 722 F.2d 695 (11th Cir. 1984); Simon v. Commissioner, 830 F.2d 499, 507, (3rd Cir. 1987); Madison Gas & Electric Co. v. Commissioner, 72 T.C. 521, 564-65 (1979), aff'd. 633 F.2d 512 (7th Cir. 1980). In order to divine the intent of a partnership the courts have focused "on the motives and objectives of the promoters and general managers of [the partnerships]". Surloff v. Commissioner, 81 T.C. 210, 233 (1983); Rosenfeld v. Commissioner, 82 T.C. 105, 112, 113 (1984).

In determining the existence of a partnership's profit motive, the Tax Court has stated:

> In the case of [the partnerships], however, much of

> our focus must be on Resource, which, though not the general partner of either partnership, in effect ran both of these partnerships' affairs. The nominal general partners of [the partnerships] were Romero and Markovitz, respectively, but the record is clear that for expertise, purchase negotiations and partnership management, these men merely relied on Resource to do all that was necessary. [Fox v. Commissioner, 80 T.C. 972 (1983) aff'd sub nom. Barnard v. Commissioner, 731 F.2d 230 (4th Cir. 1984)].

The question of whose mental state must be examined in order to determine the existence of a profit motive is a question of law, reviewable de novo. See, Campbell v. Commissioner, 868 F. 2d 833 (6th Cir. 1989); Simon v. Commissioner, 830 F.2d 499, 501 (3d. Cir. 1987).

The Tax Court relied heavily on the testimony of Michael Zukerman, the attorney who presided over the drafting of the Partnerships' private placement

memorandum in finding that the Koppelman Process activity was primarily tax motivated. There is no evidence that Zukerman acted other than as a legal advisor to the promoters and the Partnerships. He was not in control of the Partnerships. He was not involved in making the business decisions which led to the formation of the Partnerships.[4]

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[4]He specifically testified that he did not participate in the negotiation of the license fees paid to Sci-Teck. He also testified as follows:

Q.... You know Keith Gaskell?

A. Yes.

Q. And his role in this was to put many-- get information and put many aspects of this together on behalf of the two limited partnerships which it was intended would be created; is that right?

A. Yes.

Q. You, on the other hand, represented whom?

A. The partnership. The partnership.

Q. In other words, what you were doing overlapped in many respects to what Keith Gaskell was doing, is that what you're saying?

A. Yeah, we were the lawyers and he would be the businessman.

He was merely fulfilling his legitimate legal role which included advice to the promoters as to methods of tax minimization. After the Partnerships were formed there is no evidence that he played any role at all. It was thus improper as a matter of law for the Tax Court to rely on Zukerman's testimony as the "primary evidence" for its decision that the Partnerships lacked a profit objective.

The 11th Circuit excused this reliance by the Tax Court by finding that the Tax Court used Zukerman's testimony in its determination of whether the transactions lacked economic substance rather than in determining the taxpayers' subjective motivation. However, under Rice's Toyota World v. Commissioner, 752 F.2d 89, 91 (4th Cir. 1985), a

transaction will not be ignored as a sham unless it lacks business purpose, <u>and</u> the transaction has no economic substance because no reasonable possibility of a profit exists. Zukerman's testimony only goes to subjective motivation. Nothing in his testimony addressed the question of whether the transactions had a reasonable possibility of earning a profit.

IV. <u>Without Regard To Whether The Koppleman Process Activity Was A Sham, Interest On The Partnership Notes Is Deductible.</u>

A portion of the consideration due to Sci-Teck and FTRD consisted of notes payable by POGA to those entities. POGA accrued interest on the notes, and the Karrs deducted their pro rata share of

the interest on their income tax return. The Tax Court disallowed this deduction stating, "there is every reason to believe that the partnership would never have funds available to pay the interest on the notes. The interest, therefore, is too unlikely to be paid to be deducted on an accrual basis." In the companion case of Smith, the Sixth Circuit reversed the Tax Court, holding that the notes were genuine, and therefore interest on them was deductible. However, in the instant case the 11th Circuit upheld the Tax Court's ruling.

Even where a transaction is disregarded as a sham, interest expense is deductible on a note provided the obligation is genuine. Rice's Toyota World, Inc. v. Commissioner, 752 F.2d at 96; Smith v. Commissioner 937 F.2d. 1089,

1098 (1991). "[D]eductions for accrued interest are proper where it can not be categorically said that the interest would not be paid, even though the course of conduct of the parties indicated that the likelihood of payment of any part of the disallowed portion was extremely doubtful." Cohen v. Commissioner, 21 T.C. 855, 857 (1954) (citations omitted); See Rev. Rul. 70-367, 1970-2 C.B. 37.

The notes, including interest, were payable not only from any income from the exploitation of the Koppelman Process, but also out of the oil and gas operations. In 1981 the Partnerships prepared an analysis of expected revenue from gas and oil well drilling operations. The Tax Court found that "the projected revenues from gas and oil well drilling would have been sufficient

to completely retire the partnerships' notes to Sci-Teck and FTRD both as to principal and interest." (Emphasis supplied).

Oil and gas expert, Jeffrey Lam, testified at trial that the assumptions used by the Partnerships to calculate the projected revenues and cash flow set forth in the analysis were reasonable and consistent with industry practice, and that in his opinion the projections set forth by the Partnerships were reasonable. The Tax Court held that this was the only testimony as to the likelihood of the notes being paid. Based upon the projections there was a reasonable probability that the interest accrued in 1982 (the only year before the Court in which POGA accrued and deducted interest) would have been paid in 12

years. As the chart reproduced as Appendix G illustrates, during 1982 interest of $2,192,625[5] accrued on a principal balance of $35,493,750.[6] As the chart also demonstrates, revenues from the oil and gas operations would have been applied to the accrued interest beginning in 1982[7], and by 1994 virtually the entire amount of interest accrued would have been paid.

Thus, the uncontradicted evidence is that the accrued interest would have in

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[5]Simple interest of 6 per cent was accruing on the notes to Sci-Teck and FTRD.

[6] Based on 250 units being sold.

[7]The chart is extrapolated from the projections prepared by POGA in 1981 which Jeffrey Lam found to be reasonable. As called for in the offering memorandum twelve per cent of the payments applied to the notes are applied to interest.

all probability been paid within 12 years, not 25 as stated by the Court. While it is true that events might have occurred (and did in fact occur) which would prevent payment of the interest, this does not prevent accrual. The "potential non-payment of an incurred liability exists for every business that uses an accrual method, and it does not prevent accrual." United States v. Hughes Properties, Inc., 476 U.S. 593, 606, 106 S.Ct. 2092, 2099 (1986).

All of the evidence indicates that it was reasonable to believe that the notes, including interest would have been paid without regard to the success or failure of the Koppelman Process. The Tax Court's finding to the contrary was clearly erroneous. In addressing these arguments the Eleventh Circuit's only

response was, "[b]ecause the interest on the notes was payable only out of POGA's anticipated revenues, and payment was not due for twenty-five years, the Tax Court did not clearly err in finding that the obligation was to contingent to meet the standards for accruability." This statement is both factually and legally incorrect.

As noted above the only evidence in the record as to the payment of interest demonstrated that all of the accrued interest would be paid in twelve years. The courts have generally permitted a deduction under the all-events test, even if the liability would not be discharged until the distant future. Illinois Power Company v. Commissioner, 87 T.C. 82 n.28 (1986) (and cases cited therein); Mooney Aircraft, Inc. v. United States, 420 F.2d

400 (5th Cir. 1970). As the Tax Court stated in Illinois Power Company:

> In the instant case, we need not decide whether a liability paid 40 years after accrual rises to the level of a "practical nullity" because, as of the end of 1981, there was a reasonable expectation the liability would be paid well before the end of the lease.

Like Illinois Power Company, this case involves a "reasonable expectation" that the liabilities in question would be paid over a relatively short period of time. Nothing more is required to accrue the interest obligation.

In Mooney Aircraft, Inc. v. United States, 420 F.2d 400 (5th Cir. 1970) the government argued that the length of time (20 years or more) until the notes were due prevented accrual. The 5th Circuit specifically rejected the Commissioner's argument that the obligations in question did not meet the all-events test. Id at

405. Even though the 5th Circuit held that the expenses involved could not be deducted, it did so based upon its determination that the Commissioner did not abuse his discretion under Internal Revenue Code Sec. 446(b) to disallow any accounting method which does not clearly reflect income. Id at 406.

In the present case, the Commissioner has never contended, and the lower courts have never held that the Partnerships' method of accounting resulted in a distortion of income. Whether an accounting method materially distorts income is a question of fact. Van Raden v. Commissioner, 71 T.C. 1083, 1104 (1979). It would be extremely prejudicial to allow this argument to be raised at this late stage in the proceedings, since no factual record on

this point was created at trial.

V. The Eleventh Circuit's Decision That The Taxpayers' Did Not Have Reasonable Cause For The Understatement On Their Tax Returns Is Contrary To The Position Of This Court.

Even if the 11th Circuit's decision as to the tax deficiency was correct, its decision to uphold the penalty imposed pursuant to Section 6661 is at odds with the principals expressed by this Court in United States v. Boyle, 469 U.S. 249, 105 S.Ct. 687 (1985). The law provides an addition to tax of 10 per cent of the understatement of any tax liability if the understatement is substantial. Section 6661.[8]. The Commissioner of

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[8]After the Commissioner mailed his notice of deficiency the rate of the addition to tax was increased to 25 per

Internal Revenue has the authority to waive an otherwise applicable addition to tax pursuant to section 6661, if there was reasonable cause for the understatement, and the taxpayer acted in good faith. Section 6661(c). A failure by the Internal Revenue Service to waive the addition to tax pursuant to section 6661 is reviewable by the Tax Court, and may be set aside where the Commissioner's decision is arbitrary, capricious or without sound basis in fact. Mailman v. Commissioner, 91 T.C. 1079 (1988). The Tax Court decided below that it did not need to examine the limits of the Commissioner's discretion in failing to

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cent. See Pallottini v. Commissioner, 90 T.C. 498 (1988). The Commissioner conceded that the addition to tax was limited to ten per cent because he did not make a claim for the increased amount.

grant a waiver since, under its view of the facts, there was no showing that there was reasonable cause for the understatement or that the taxpayers acted in good faith.[9] The 11th Circuit did not use the proper standard in determining that the taxpayers did not have reasonable cause or act in good faith. In United States v. Boyle, 469 U.S. 249 (1985), this Court reviewed de novo whether an executor's reliance on his attorney's assurance that a tax return would be filed on time constituted "reasonable cause" for failing to timely file an estate tax return. This Court

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[9]In instances where there is a determination by the courts that the Commissioner acted without rational basis in issuing a notice of deficiency, it has been held that the burden of proof shifts to the Internal Revenue Service. LeBow v. Commissioner, 763 F.2d 125, 132 (2d Cir. 1985); Llorente v. Commissioner, 649 F.2d 152, 156 (2d Cir. 1981).

stated:

> A number of courts have indicated that "reasonable cause" is a question of fact, to be determined only from the particular situation presented in each particular case. This view is not entirely correct. Whether the elements that constitute "reasonable cause" are present in a given situation is a question of fact, but what elements must be present to constitute "reasonable cause" is a question of law. When faced with a recurring situation, such as that presented by the instant case, the courts of appeals should not be reluctant to formulate a clear rule of law to deal with that situation. [United States v. Boyle, 469 U.S. at 249, n.8] [emphasis in original] [citations omitted].

The Court went on to find that relying on an attorney to file a tax return was not reasonable cause, since it requires no special training or expertise to ascertain the filing date of a return and ensure that it is met. The Court, however, distinguished the situation where a taxpayer relies on the

substantive legal advice of an attorney or accountant with regard to the interpretation of the tax laws. United States v. Boyle, 469 U.S. at 250, 251, 687 S. Ct. at 692. In the later circumstance the Court stated:

> When an accountant or attorney advises a taxpayer on a matter of tax law, such as whether a liability exists, it is reasonable for the taxpayer to rely on that advice. Most taxpayers are not competent to discern error in the substantive advice of an accountant or attorney. To require the taxpayer to challenge the attorney, to seek a "second opinion," or to try to monitor counsel on the provisions of the Code himself would nullify the very purpose of seeking the advice of a presumed expert in the first place. "Ordinary business care and prudence" do not demand such actions. [citation omitted] [emphasis in original] [United States v. Boyle, 469 U.S. at 251, 687 S. Ct. at 692, 693].

It is this duty to second guess counsel, which the Eleventh Circuit has imposed on the taxpayers. The

transactions entered into by the Partnerships, and the tax provisions governing them were complex. The taxpayers relied on their accountant in preparing their tax returns. Their financial planner reviewed the offering memorandum[10] prior to their making an investment in POGA. In addition, the taxpayers had every reason to believe their accountant's treatment of the partnership losses on their tax return was correct since prior to filing their tax returns they had received a letter from the "big 8" CPA firm of Fox and Company assuring them that the deductions

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[10]The tax opinion did not state that the deductions were unavailable. In fact it set forth the opinion of the law firm of Baskin and Sears to the contrary. It merely acknowledged that the Internal Revenue Service might challenge the transaction.

shown on POGAs K-1s were correct.

The 11th Circuit held that such reliance was not reasonable since the offering memorandum set forth potential challenges from the Internal Revenue Service, and the letter from Fox & Company warned of the possibility of the substantially understatement penalty being imposed. Thus, in the view of the 11th Circuit the taxpayers were required to read and assimilate the tax opinion set forth in the memorandum, and debate their accountants as to whether or not the losses were deductible. According to this Court ordinary business care and prudence do not require a taxpayer to go that far.

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